No. 96-324

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Supreme Court of the United States

October Term, 1996

JOHNSIE RILEY, on behalf of herself and all others similarly situated; JOHN F. RILEY, on behalf of himself and all others similarly situated; VIRGINIA HARRINGTON, on behalf of herself and all others similarly situated; DEWEY HARRINGTON, on behalf of himself and all others similarly situated,

Petitioners,

v.

DAVID H. MURDOCK; DHM HOLDING CORPORATION; MURDOCK INVESTMENT CORPORATION; PACIFIC HOLDING CORPORATION; CANNON HOLDING CORPORATION,

Respondents.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fourth Circuit

PETITIONERS' REPLY BRIEF

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Respondent's Brief In Opposition To the Petition For Writ Of Certiorari confirms that there is a conflict among the circuits on the application of ERISA fiduciary duties to the purchase of a plan termination annuity and that the record below created triable issues of fact, thus highlighting the need for review by this Court.

I. Respondent's Brief Disputes The Facts, Thus Confirming The Impropriety Of Summary Judgment On The Issue Of Whether Murdock Breached The Duty Of Prudence.

Throughout Respondent's Brief, Murdock challenges the Plaintiffs' Statement Of The Case and urges this Court to view the facts that he presents through his own peculiar prism. Despite the accusation of "distortion or outright misrepresentation," Respondent's Brief at 1, Respondent's Statement of the Case really argues that Respondent would draw different inferences from the record, which he incompletely and inaccurately relates.

A. Respondent Concedes The Existence Of Facts Available To The Fiduciary That A Prudent Investigation Would Have Uncovered.

One factual argument that Respondent makes is that "the Committee upon which Murdock relied thoroughly investigated this precise issue. . . . " Respondent's Brief at 5. Respondent's Brief is unclear about what precise issue was thoroughly investigated by Murdock's Committee. Moreover, the motions that the Committee may have gone through to do its supposed investigation (which Plaintiffs do not concede was either substantial or independent) are not the sole measure of prudence. Rather, as

the Third Circuit recently concluded, "the thoroughness of a fiduciary's investigation is measured not only by the actions it took in performing it, *but by the facts that an adequate evaluation would have uncovered.*" *In re Unisys Savings Plan Litigation*, 74 F.3d 420, 436 (3d Cir. 1996), *cert. denied*, 1996 US LEXIS 4673 (October 7, 1996) (emphasis supplied) (citing *Fink v. National Savings and Trust Co.*, 772 F.2d 951, 962 (D.C. Cir. 1985) (Scalia, J. concurring in part and dissenting in part)).

Under the measure of prudence set forth in *Unisys*, the facts available to the Plan fiduciaries when they performed their investigation are material to the ultimate resolution of the issue of whether Murdock breached his duty of prudence. Respondent concedes that these facts included those disclosed in Executive Life's public filings, such as Executive Life of California's 1983, 1984 and 1985 NAIC annual statements, Executive Life of New York's 1983, 1984 and 1985 NAIC annual statements, and the 10-K's of Executive Life's parent, First Executive Corporation, for 1983, 1984 and 1985. Respondent's Brief at 8 n.2 (making reference to the report of one of Plaintiffs' experts at JA 438, 451). Respondent also recognizes the existence of an April 17, 1986 memorandum by Hewitt Associates, expressing at least "four 'potential negatives' [about Executive Life] which were 'worth monitoring.' " Respondent's Brief at 4; JA 267-270. The availability of such information, not the number of times that the Committee waved a "magic wand" over the transaction, *see Roth v. Sawyer-Cleator Lumber Co.*, 16 F.3d 915, 918 (8th Cir. 1994), determines the thoroughness of the investigation and whether the duty of prudence was satisfied.

Another factual argument that Respondent makes is that "[v]irtually all negative ratings of Executive Life or

adverse action by state regulatory authorities occurred after July 1986." Respondent's Brief at 17. This carefully worded statement, addressing negative ratings but not the other negative information that abounded before July, 1986, is belied by Murdock's own brief. In addition to the references to public disclosures discussed above, Respondent's Brief at 2-3 addresses the report of the California Department of Insurance, determining that Executive Life was statutorily insolvent in 1984, two years before the annuity purchase. In a list of documents supporting his report, one of Plaintiffs' experts notes that this report of examination was released to the public on 11/14/85, and was circulated earlier. (JA 451). Nonetheless, Respondent attempts to cast the determination of statutory insolvency as "purely a technical issue." Respondent's Brief at 3.

Obviously, the parties disagree about the facts that an adequate evaluation would have uncovered and the inferences to be drawn from the evidence. Indeed, Petitioners can controvert each and every "fact" proffered by Respondent. However, Petitioners recognize that this forum is not the place to resolve factual disputes. The simple points are: (1) the Courts below applied a standard of prudence that is different from the one applied by the Third Circuit in *Unisys*, thus demonstrating a conflict in the circuits; and (2) the parties' differing views of the facts and inferences concerning information available to the Plan fiduciary confirm that there are genuine issues of material fact and that Respondent was not entitled to judgment as a matter of law.

B. Respondent's Brief Raises The Conflict In The Circuits On The Continuing Duty To Monitor Applicable To A Fiduciary's Purchase Of A Plan Termination Annuity.

Respondent recognizes another conflict between this case and *Unisys* regarding the duty of prudence. Respondent's Brief at 18 concedes that one holding of *Unisys* is that in the context of an ongoing plan, a fiduciary has a continuing duty to monitor the investments. Respondent argues, however, that no such duty applies in the purchase of a group annuity contract upon termination of a plan, in part because he would have been powerless to change the annuity provider.[1] Respondent's Brief at 18.

Respondent's Brief concedes that additional negative information became publicly available between July, 1986, when Respondent accepted Executive Life's bid, and October, 1986, when the reversion was distributed to him. *See, e.g.*, Respondent's Brief at 2, 8 n.2, referencing the 1986 Best report and Conning & Company reports. Thus, after this additional information became known, the Plan still had approximately $38 million in assets, and steps could have been taken to protect the interests of the participants and beneficiaries. (JA 298). Nonetheless, according to Respondent, a fiduciary can, as a matter of law, ignore negative information about an annuity provider after he has accepted the bid, even though he later received millions of dollars in "surplus" assets with which additional security could be purchased.

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[1] Petitioner had urged below that there was some duty to monitor after an annuity purchase and that there were facts supporting such a duty in this case. Petition at 5; Brief of Appellants at 18-19, 33-34.

Respondent's attempt to distinguish *Unisys* on this issue is unavailing, and Respondent's Brief raises yet another aspect of the duty of prudence on which the Third and Fourth Circuits conflict and on which summary judgment was inappropriate.

* * *

In short, Respondent's Brief supports Petitioners' contention that the opinions of the Courts below created a conflict in the circuits and that the Courts below erred in granting summary judgment.

II. By Admitting That Price Was One Of Three Critical Factors In The Annuity Selection, Respondent Highlights The Conflict On The Application Of The Duty Of Loyalty.

Respondent expressly concedes that: (1) price was a critical criterion for his selection of an annuity provider (Respondent's Brief at 10); (2) ERISA forbids an annuity selection which is "excessively motivated by price" (Respondent's Brief at 21); and (3) the Ninth Circuit correctly held in *Pilkington PLC v. Perelman*, 72 F.3d 1396 (9th Cir. 1995), that a large price differential is "enough to raise a triable issue" concerning whether the fiduciary's motivation deviated from that mandated by ERISA. *See Pilkington*, 72 F.3d at 1401. Respondent argues, however, that because Executive Life's winning bid was "only $500,000" less than the second lowest bid, "price obviously was not a significant consideration." Respondent's Brief at 11, 21.

Thus, Respondent attempts to harmonize this case with *Pilkington* by contending, in effect, that a fiduciary is

always permitted to be guided by his own pocketbook as long as his gains are not so "dramatic" as to make the influence on his choice "excessive," and that as a matter of law, an additional $500,000 profit is too trivial to be a significant factor.

There are three major flaws in Respondent's theory. First, the record does not support Respondent's claim that he only realized an extra $500,000 by choosing Executive Life. Rather, the actual differential appears to have been substantially in excess of $2 million. (*See* JA 298, 952-54, 1029).[2] Second, Respondent can point to no reason or authority for drawing the line of materiality at $500,000 or $3 million or any other arbitrary figure.[3] Third, the language, structure and purpose of ERISA do not permit *any* level of self-interested motivation by a fiduciary, but rather require a fiduciary to act solely in the interest of the plan participants and beneficiaries and for the exclusive purpose of providing benefits, in choosing a plan termination annuity. Thus, under ERISA, plan

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[2] Moreover, the important price difference is not necessarily between the two lowest bids; rather it is the difference between the winning bid and the price of the annuity which would have been selected if the participants' and beneficiaries' interests were the sole criteria. At least three companies submitted bids that were more than $10 million higher than Executive Life's winning bid, and the record reveals no non-price reason for rejecting these companies. (*See* JA 298, 952-54, 1029).

[3] Indeed, the Courts below did not even attempt to draw any such line, but instead mistakenly assumed that a prudent investigation would in itself satisfy the duty of loyalty, without regard to the motivating influence of any price differential. *See* Petition at 16.

fiduciaries should be required to engage in some comparative analysis of the relative safety of available annuity providers, rather than simply considering competitive pricing.

For this reason, the Department of Labor is correct in interpreting the duty of loyalty as requiring, in the context of a plan termination annuity, that a fiduciary seek the safest available annuity to assure payment of the benefits which the plan promised to its participants. The Department of Labor's interpretation, now codified at 29 C.F.R. § 2509.95-1, favors the participants and beneficiaries over the fiduciary, and is the only proper accommodation of the parties' interests in light of ERISA's duty of loyalty. Respondent's attempt to create a safe harbor in which a fiduciary may favor his own interest without judicial scrutiny is patently inconsistent with ERISA and highlights the fundamental conflict between this case and *Pilkington*.[4]

Respondent's discussion of the duty of loyalty uncovers the glaring conflict between the decision of the Courts below and the decision of the Ninth Circuit in *Pilkington*. Review by this Court is needed to resolve this

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[4] Respondent also recognizes that the *Pilkington* fiduciaries had a quid pro quo relationship with Executive Life, which contributed to the Ninth Circuit's view that there were triable issues of fact on the duty of loyalty. He then concedes that there is similar evidence in this case, but dismisses the "overlap" in Executive Life's portfolio and Murdock's companies as *de minimis*. Respondent's Brief at 22 n.3. As in Respondent's discussion of the price differential, his discussion of quid pro quo relationships shows that there is a conflict between *Pilkington* and the decision of the Courts below.

conflict and reassert the inviolability of the duty of loyalty.

III. Contrary To The Law Of Every Other Circuit, Respondent Argues That A Fiduciary Who Profits From The Breach Of Fiduciary Duties Need Not Disgorge His Unjust Enrichment.

Respondent states that after a temporary shortfall, he made up the loss in benefits that occurred upon the demise of Executive Life. Respondent's Brief at 1. Respondent thus concedes that the participants' security, which ERISA was enacted to protect, has been jeopardized. Despite this fact, the Fourth Circuit refused to examine whether the Plan fiduciary breached his duties under ERISA § 404 because it determined that the Plan participants received their benefits. (App. 3).

As set forth in the Petition at 18-19, the analysis employed by every other circuit is otherwise. This Court should grant the writ to resolve the conflict created by the holding of the Courts below, in refusing to hold Respondent accountable for gains attributable to his breaches of fiduciary duty.

IV. Respondent's Attempt To Justify The Exclusion Of Plaintiffs' Experts Demonstrates The Error Of The Courts Below.

Respondent's discussion of the exclusion of Plaintiffs' experts reveals the error of the Courts below. First, Respondent's Brief at 25-26 cites a line of cases, relied upon by the District Court (App. 35), to support the inadmissibility at trial of "mere" conclusory, unsupported

opinions of an expert. However, Plaintiffs proffered the expert reports in opposition to a motion for summary judgment, rather than at trial; thus, these cases are inapposite. In the Petition at 21, Plaintiffs urge that the controlling case is *M & M Medical Supplies v. Pleasant Valley Hospital, Inc.*, 981 F.2d 160 (4th Cir. 1992), *cert. denied*, 508 U.S. 972 (1993), a point essentially conceded in Respondent's Brief at 26, stating that *M & M Medical Supplies* concerned admissibility of an expert's affidavit under Rule 56(e). Thus, Respondent confirms that *M & M Medical Supplies*, and not the cases concerning admissibility of expert testimony at trial, provides the controlling standard.

Second, even if Rule 56 required that supporting data be attached to an expert report, Respondent in effect concedes that Plaintiffs' experts did rely on "events and information." Respondent's Brief at 26. Moreover, Respondent concedes that the information upon which one of Plaintiffs' experts relied included Executive Life's public filings going back to 1983. *See* Respondent's Brief at 8 n.2 and discussion at page 2 *supra*. Thus, if expert reports on summary judgment must attach the factual support for the opinion, Respondent in effect concedes that Plaintiffs' experts met that standard, unless a company's filings with the SEC and similar public disclosures are irrelevant to an expert's opinion concerning the financial condition of a company.

Third, implicitly recognizing the impropriety of the District Court's refusal to consider the reports of Plaintiffs' experts that relied on public disclosures and other information, Respondent argues that the District Court did not hold the expert reports inadmissible, but rather received and analyzed those reports and the evidence upon which

they relied. The District Court's opinion at App. 34-35 and the cases relied upon therein make clear that the Court did no such analysis. Moreover, if it did undertake an analysis of the reports and the evidence relied upon, the Court improperly made a credibility determination on summary judgment.

Thus, Murdock's argument regarding Plaintiffs' expert testimony demonstrates that the Courts below applied the wrong standard and improperly ignored the ample support for Plaintiffs' expert opinions. The treatment of Plaintiffs' experts by the Courts below was a serious departure from judicial norms and should be reviewed by this Court.

CONCLUSION

For the foregoing reasons and those in the Petition for Writ of Certiorari, a Writ of Certiorari should issue to review the judgment and opinion of the United States Court of Appeals for the Fourth Circuit.

Respectfully submitted,

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